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Ex Parte

Federal Communications Commission

Broadband Policy

and its relationship to inter-carrier compensation

January 13, 2010

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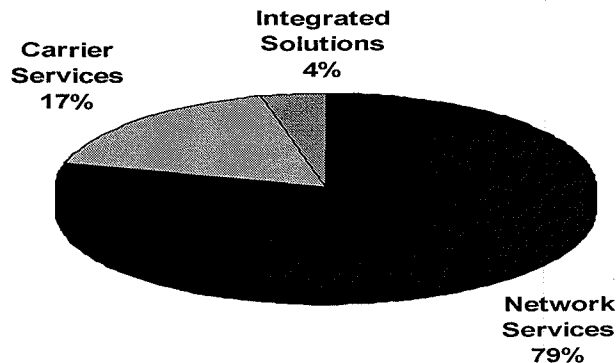
Broadband Policy and its relationship to inter-carrier compensation

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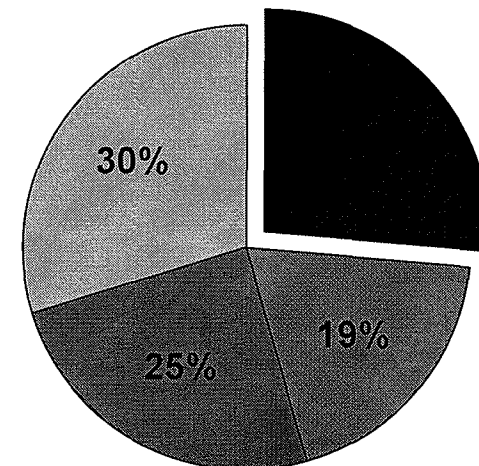
Total Revenue = \$1.6 Billion

- One of the largest Nationwide providers of Competitive Communications Solutions⁽¹⁾
- Extensive National Footprint
- Presence in 47 of the top 50; 84 of the top 100 MSAs
- Industry leading customer satisfaction
- 27 quarters of positive free cash flow generation; never restructured

2009 Revenue Composition by Service and Customer Size⁽²⁾



■ <\$1K ■ \$1K-\$2.5K ■ \$2.5K-\$10K ■ >\$10K



(1) Based upon revenue
(2) Annualized YTD Q309 Revenues

Broadband Policy and its relationship to inter-carrier compensation

Discussion Topics:

- ✓ **Broadband Policy has only a limited relationship to inter-carrier compensation.**
 - ✓ To the extent possible, the two should be pursued separately.
- ✓ **Inter-carrier compensation must be addressed comprehensively.**
 - ✓ Any statements about inter-carrier compensation in the Broadband Report may tend to further destabilize the market
- ✓ **Key inter-carrier compensation issues**
 - ✓ Any changes in inter-carrier compensation should be evaluated for impact on carriers' ability to maintain and expand broadband offerings



Broadband Policy and its relationship to inter-carrier compensation

✓ **Key inter-carrier compensation issues**

✓ **Comprehensive reform must address:**

✓ **Necessary market forces:**

If barriers to entry or other anomalies keep the market from disciplining inter-carrier compensation rates – fix those problems rather than regulatory price-setting.

✓ **Proper cost-recovery:**

If rates can and must be set by the FCC, proper cost recovery must be a key objective. While proper cost recovery can be ensured with benchmarking, must be done with care. CLECs cannot be benchmarked to AT&T, Verizon and Qwest (three of the largest, most integrated telecom firms in the world).

✓ **Special access capacity**

Special access is a key input into switched access for CLECs. Special access must be addressed as part of overall inter-carrier “capacity” purchasing reform

✓ **IXC self-help**

Rules should preclude carrier-customers from using self help to extract unlawful concessions from CLECs and smaller LECs



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Broadband Policy and its relationship to inter-carrier compensation

- ✓ Key inter-carrier compensation issues
- ✓ Comprehensive reform must address:
 - ✓ Necessary market forces:

Two wrongs do not make a right. We should correct the regulations that interfere with price signals, not enshrine price regulation forever while doing nothing to remove the regulatory barriers to exchange access services.

Commissioner Furchgott-Roth, Dissent, 7th Report and Order¹

Many barriers have dissolved, other can be removed

FCC's 2001 7th Report and Order¹ was, by its own findings, intended to be transitional until market forces could take over. The market forces it discussed (e.g., IXC/LEC alliances, IXC entry into local markets) have arrived.

¹ In the Matter of Access Charge Reform, Reform of Access Charges Imposed by Competitive Local Exchange Carriers, Seventh Report and Order and Further Notice of Proposed Rulemaking, CC Docket No. 96-262, rel. April 27, 2001. E.g., see paras. 7 and 32.

If the Commission abandoned its broad reading of section 254(g) and removed the other regulatory barriers in the long-distance markets, companies could compete for business by offering differing packages of services. Some would offer to provide all billing and collection services as well as insurance for the risk associated with the distribution of access charges. Others would offer different types of insurance, and still others would offer no insurance, instead passing all charges directly to the consumer.

Commissioner Furchgott-Roth, Dissent, pg. 6



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Broadband Policy and its relationship to inter-carrier compensation

- ✓ **Key inter-carrier compensation issues**
- ✓ **Comprehensive reform must address:**
 - ✓ **Proper Cost Recovery (if rate setting is required and legally permissible):**
 - ✓ **Total Service Long Run Incremental Cost (“TSLRIC”) is a reasonable basis for inter-carrier rate setting.**
 - ✓ There has been too large a focus on “usage sensitive” costs, soft switches, etc.
 - ✓ **Benchmarking can work – but not by benchmarking much smaller CLECs to rates of AT&T, Verizon and Qwest (three of the largest, most vertically- and horizontally-integrated carriers in the world) set via the CALLS order.**
 - ✓ **Requiring a single rate per competitor (inter-, intra-, orig-, term-, local, access, etc.) solves most issues identified by IXCs.**
 - ✓ **Costs for switched usage (especially for CLECs) do not approach zero and are substantially in excess of \$0.0007 and other benchmarks touted by the IXCs.**



Broadband Policy and its relationship to inter-carrier compensation

- ✓ **Key inter-carrier compensation issues**
 - ✓ **Comprehensive reform must address:**
 - ✓ **Proper Cost Recovery** (if rate setting is required and legally permissible):
 - ✓ While some have suggested that reduction in inter-carrier compensation can be offset by increases in USF funding, CLECs do not generally receive USF funding
 - ✓ Below-cost rates for any service result in economically inefficient overconsumption of the service (e.g., TDM-based flat-rated calling).
 - ✓ Bill and keep is inappropriate where traffic is one-way, including IXC to LEC.
 - ✓ AT&T, Sprint and Verizon agenda related to switched access is “tail wagging the dog.” Switched access advocacy is primarily a “profit” issue for large IXCs.



Broadband Policy and its relationship to inter-carrier compensation

- ✓ Key inter-carrier compensation issues
- ✓ Comprehensive reform must address:
 - ✓ Proper Cost Recovery (if rate setting is required):

**PAETEC has
studied its
switched usage
costs via QSI's
Network Usage
Cost Analysis
(NUCA) tool**



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New Jersey

RATE DEVELOPMENT

1. RATE PER MOU	\$XXXXXX	SUM(In2:In6)
2. DIRECT COST PER MOU	\$XXXXXX	In14
3. SHARED AND COMMON COSTS PER MOU	\$XXXXXX	In2 * S&C Factor
4. BAD DEBT EXPENSE	\$XXXXXX	(1+In3+L5) * BD Factor
5. LOOP COST RECOVERY	\$XXXXXX	Loop Cost Analysis / In13
6. CONTRIBUTION 0.00%	\$XXXXXX	sum(In2:In5) * Contr %

NUCA-USAGE SENSITIVE COSTS

MONTHLY DIRECT COSTS

7. TRUNK - TO - TRUNK SWITCHING	\$XXXXXX	Switching Module
8. TRANSPORT	\$XXXXXX	Transport Module
9. TRANSPORT TERMINATION	\$XXXXXX	Transport Term. Module
10. SIGNALING	\$XXXXXX	Signaling Module
11. TOTAL MONTHLY RECURRING DIRECT COSTS	\$XXXXXX	sum(In7-10)

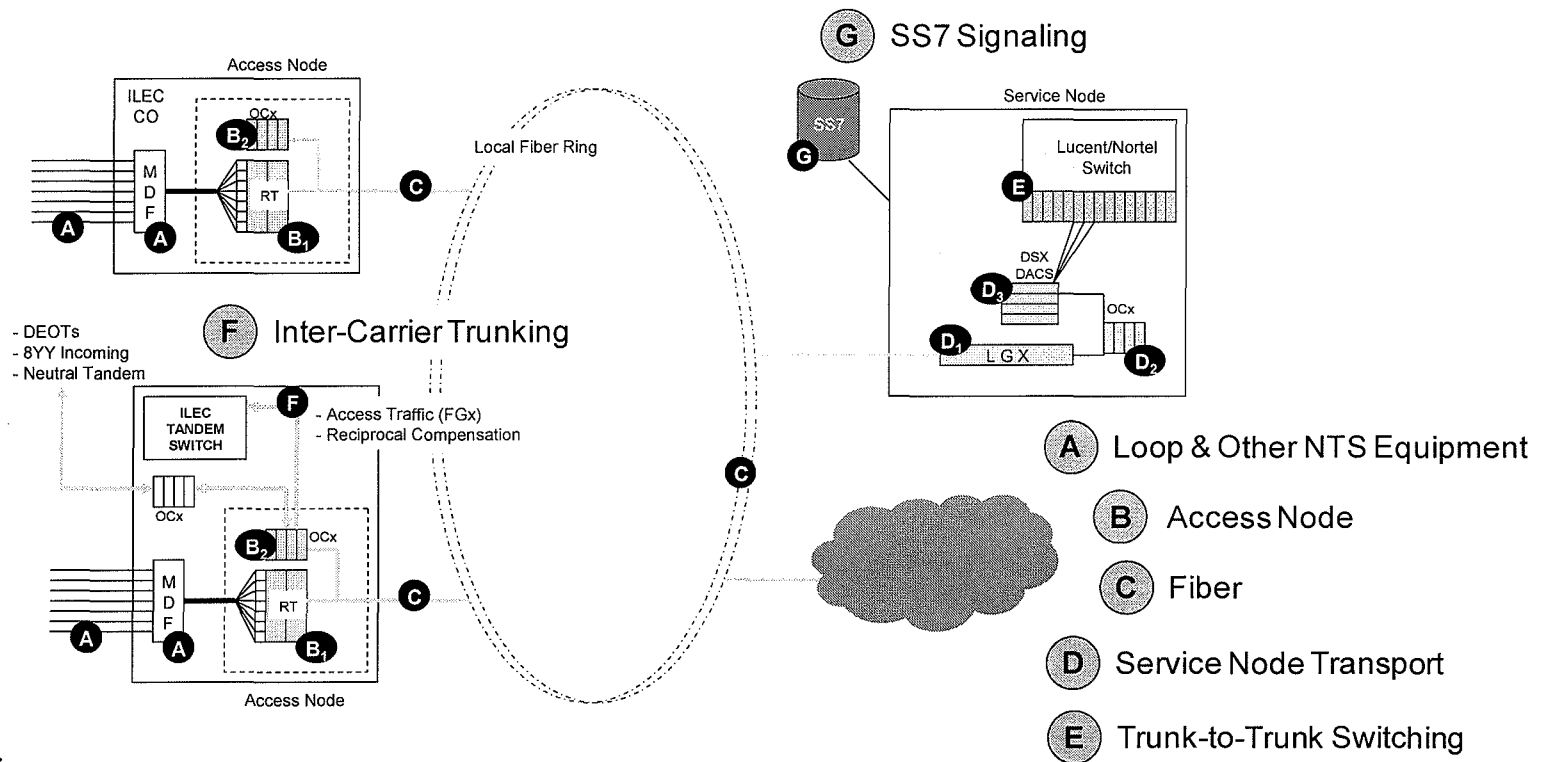
PER UNIT COSTS - DIRECT

12. TOTAL MONTHLY RECURRING DIRECT COSTS	\$XXXXXX	In11
13. TOTAL MONTHLY DEMAND (MOUS)	\$XXXXXX	Traffic Module
14. DIRECT COST PER MINUTE OF USE	\$XXXXXX	In12 / In13

Broadband Policy and its relationship to inter-carrier compensation

- ✓ Key inter-carrier compensation issues
- ✓ Comprehensive reform must address:
 - ✓ Proper Cost Recovery (if rate setting is required):

NUCA is a TSLRIC analysis customized specifically to the PAETEC network

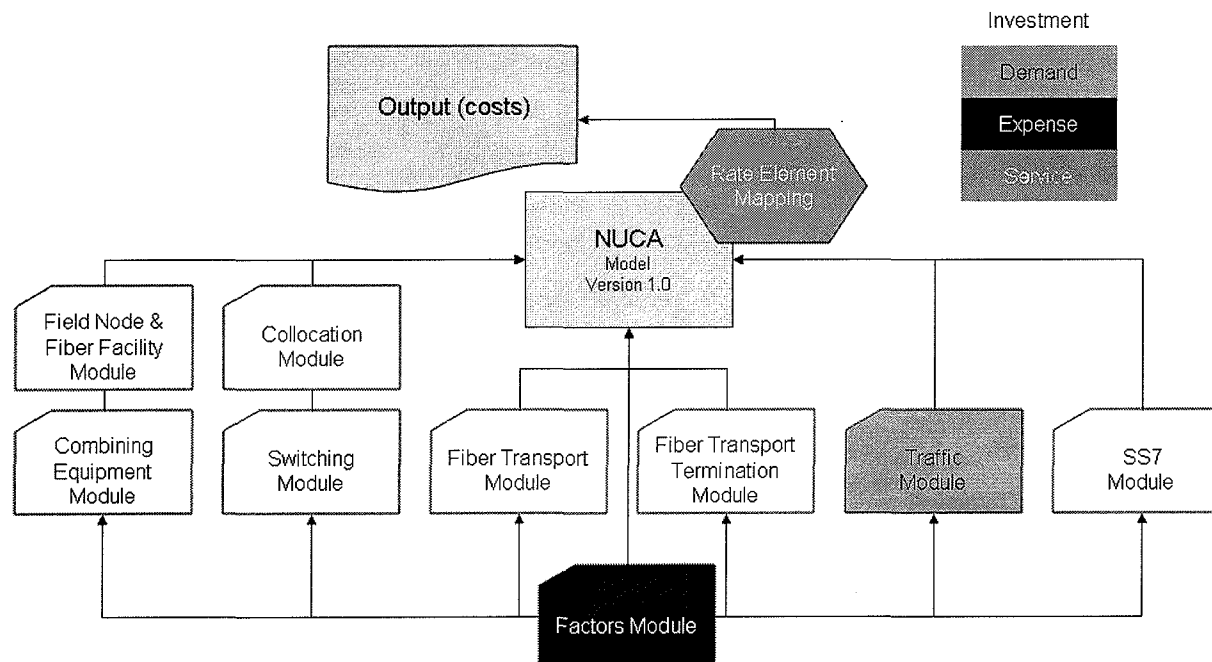


Broadband Policy and its relationship to inter-carrier compensation

- ✓ Key inter-carrier compensation issues
 - ✓ Comprehensive reform must address:
 - ✓ Proper Cost Recovery (if rate setting is required):

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- | | |
|--|--|
| 1. Captures Traffic Sensitive Costs | 3. Maps “elements” to “functions” |
| 2. Views the network in terms of individual “elements” or assets | 4. Combines and maps functions to services |
-

Network Usage Cost Analysis (NUCA)
Flow Chart



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- ✓ **Key inter-carrier compensation issues**
- ✓ **Comprehensive reform must address:**

- ✓ **Special access capacity**

Special access is a key input into switched access (especially for CLECs). Special access must be addressed as part of overall inter-carrier “capacity” purchasing reform

- ✓ **IXC self-help**

- ✓ **FCC rules require carrier-customers to pay, under protest, for tariffed services duly performed, and then seek redress**
- ✓ **FCC should adopt a minimum forfeiture penalty for self-help violations by customer-competitors**

